VZCZCXRO2921
RR RUEHTRO
DE RUEHAS #1172/01 3091734
ZNR UUUUU ZZH
R 041734Z NOV 08
FM AMEMBASSY ALGIERS
TO RUEHC/SECSTATE WASHDC 6562
INFO RUEHBP/AMEMBASSY BAMAKO 0738
RUEHEG/AMEMBASSY CAIRO 1097
RUEHMD/AMEMBASSY MADRID 9077
RUEHNK/AMEMBASSY NOUAKCHOTT 6544
RUEHFR/AMEMBASSY PARIS 2910
RUEHRB/AMEMBASSY RABAT 2556
RUEHTRO/AMEMBASSY TRIPOLI
RUEHTU/AMEMBASSY TUNIS 7409
RUEHNM/AMEMBASSY NIAMEY 1751
RUEHCL/AMCONSUL CASABLANCA 3561
RHMFISS/HQ USEUCOM VAIHINGEN GE
RUCPDOC/DEPT OF COMMERCE WASHDC
RUEATRS/DEPT OF TREASURY WASHDC

UNCLAS SECTION 01 OF 03 ALGIERS 001172

SIPDIS

CAIRO PASS TO TREAS ASEVERENS

E.O. 12958: N/A
TAGS: EFIN EINV ECON PGOV AG
SUBJECT: 2009 GOVERNMENT BUDGET PAINTS ROSY PICTURE

REF: A. ALGIERS 930
¶B. ALGIERS 1003

¶1. SUMMARY. The Algerian parliament approved the government's 2009 budget with few amendments. Spending will increase six percent over 2008 levels, and the budget law estimates economic growth of 4.1 percent overall and 6.6 percent outside of the hydrocarbons sector. The budget uses an oil reference price of USD 37 per barrel, and while the finance minister defended the budget as sustainable in the short-to-mid term, he, the prime minister and the president each have expressed concerns publicly that the falling price of oil might negatively affect Algeria's economy and may force the government to draw from its hydrocarbons revenue regulation fund in order to balance future budgets. The government included in the 2009 finance law new measures aimed at encouraging new investment, combating fraud, simplifying the tax system, and guaranteeing taxpayer rights. But the law's assumptions regarding oil prices, combined with the Algerian economy's continued dependence on oil and gas revenues, may force the government to run bigger deficits or make tough choices to balance the budget. END SUMMARY.

BUDGET PASSED WITHOUT A FIGHT

¶2. The Algerian parliament has approved the 2009 finance law that includes the government's budget as well new fiscal measures and government policies. The finance law, defended at parliament by Finance Minister Karim Djoudi, easily passed each house with few amendments and included increased benefits for those who fought in the 1950s Algerian war for independence (known as the "moudjahidine"). Parliament left intact a controversial tax on new car sales. Action to eliminate the tax was anticipated in the lower house when it took up the finance law on October 23. The car tax, seen by many Algerians as an attack on the working class, created an uproar in the press and among opposition lawmakers when implemented in August as part of the 2008 supplemental budget (ref A). But an opposition party deputy announced that instead of an amendment to the budget law, MPs would issue a recommendation to the government to evaluate and reconsider the tax after one year.

¶3. The decision by the National Popular Assembly (APN) to avoid controversy and pass the finance law with no significant changes drew almost no derogatory headlines, save

the October 25 edition of the French-language daily L'Expression that included a headline "deputies approve antisocial measures" in reference to the failure to repeal the car tax. Even the Trotskyist Worker's Party Secretary General, Louisa Hanoune, who is usually on the front line of government-bashing within the APN, managed to draw only a small story in the state-run daily El Moudjahid on October 27, where she was quoted as saying budget amendments made by her party had been rejected in a "dogmatic manner," and that the budget benefited only the rich. The upper house, the Council of the Nation, passed the finance law with little fanfare on October 29 and President Bouteflika is expected to sign it in December.

THE NUMBERS

¶4. The 2009 finance law anticipates economic growth of 4.1 percent overall, and 6.6 percent outside the hydrocarbons sector. Inflation is projected to average 3.5 percent. The government expects to receive USD 80 billion in oil and gas revenues in 2008 while spending USD 34 billion on imports, and the budget anticipates a 10-percent increase in imports for 2009. Overall government spending for 2009 will increase 6.3 percent over 2008 levels, due in part to increases in government salaries and new hires, increased benefits to the moudjahidine, and price supports for water, wheat and milk. This will result in a USD 40 billion dollar budget deficit even as tax revenues outside of the hydrocarbons sector are expected to increase by 10 percent over 2008 levels.

¶5. The 2009 budget provides increases for every ministry except three: the Ministry of Transportation will receive a two-percent budget cut from 2008; the Ministry of Work, Employment and Social Security will suffer a 23-percent budget reduction; and the Ministry of Water Resources will see the largest budget cut at 32 percent. These budget cuts follow policy trends as the government's previous five-year public works plan draws to a close in 2009, and ongoing privatization efforts and a growing private sector have allowed the government to reduce its share of workers' benefits payments. The biggest winner among ministries will be the Ministry of Energy and Mines, who will see its budget grow by 67 percent as it strives to expand oil and gas development in the desert and finish pipeline and other gas projects on the coast. Most other agencies will experience a budget increase of between 10 and 17 percent over 2008 levels.

THE EFFECTS OF OIL PRICES

¶6. The 2009 finance law uses an oil reference price of USD 37 per barrel to project government revenues, up from USD 19 used for the initial 2008 budget. In general, any added revenue gained from a positive difference between the reference price and the actual price of oil is to be deposited into the hydrocarbons revenue regulation fund. As he defended the 2009 finance law before parliament, Finance Minister Djoudi stated that a budget based on the USD 37 reference price is sustainable for the short-to-mid term, but that over time it may be necessary to draw from the regulation fund to balance the budget. In fact, Djoudi, Prime Minister Ouyahia and President Bouteflika have each stated publicly in recent weeks that Algerians should brace for some sort of economic shock associated with the falling price of oil, and Djoudi told parliamentarians that he has created a special commission charged with monitoring domestic economic effects of the drop in oil prices.

¶7. Business leaders told the Ambassador and visiting NEA/MAG Director on November 3 that revenues based on USD 37 per barrel of oil probably cannot sustain the government given its spending priorities. A former minister said it was possible for Algeria to maintain budgets for two or three

years using the current reference price, but suggested that the government should consider basing its budget calculations on natural gas prices rather than oil prices because gas is becoming the more important hydrocarbon export commodity for Algeria. A leading bank president said he did not feel that the USD 37 marker as used in the finance law is an accurate budget reference price. The online news journal Tout sur l'Algerie on November 1 was less forgiving: it claimed that well-informed, anonymous sources confirmed that the government is actually using a reference price of USD 75 per barrel for internal calculations, and since prices have already dipped to near USD 60 on several occasions, Algeria will likely face a larger-than-expected budget deficit in ¶2009. The journal also reported that the government has already transferred more than USD 40 billion from the hydrocarbons revenue regulation fund to balance its budget in ¶2008.

OTHER PRIORITIES

¶8. The 2009 finance law also contains several legislative measures designed to spur investment and curb tax evasion and fiscal fraud. The law would establish a new investigative service under the direction of the tax administration while enhancing taxpayer rights by delineating new rules of conduct for tax inspectors. It codifies the recent imposition of a 15-percent tax on the transfer of revenues made in Algeria by companies not domiciled here, while extending tax breaks on capital gains from stock transactions and expanding broader micro-credit incentives.

COMMENT: PREPARING FOR THE END OF OIL... OR NOT
-- --

¶9. In his November 1 Revolution Day speech, President Bouteflika said the Algerian economy "is at a crossroads," and that Algerians must "face an economic earthquake" caused by the global financial crisis that will continue to shake weak economies of the developing world. Meanwhile, just as Finance Minister Djoudi warned of serious budgetary consequences if oil prices drop below USD 67 for sustained periods of time, Prime Minister Ouyahia told reporters that it is time for Algeria to prepare for a post-oil era. Yet, while Algerian leaders seem to be resolved that they cannot rely on sky-high oil prices to fill government coffers and pay for expansive public works projects, they offer little in terms of concrete measures to diversify the economy. The incentives packages and tax modernization plan, while beneficial, will do little to attract significant new foreign or domestic investments outside of the oil and gas industry.

¶10. Until measures are taken to modernize the financial sector and reform the government bureaucracy, Algeria must continue to rely on oil and gas sales -- which make up almost 99 percent of exports -- as its chief source of revenue, even as the prices of those commodities have become volatile. Furthermore, in each of the last two years, the government has burned through its annual budget within six months: supplemental budget laws were passed in the summers of 2007 and 2008 that generally adjusted upward projected government expenditures across the board. If the same pattern holds true for 2009, Algeria's budget deficit will likely exceed the projected USD 40 billion figure by 10 percent or more. We have reported that the Algerians feel vindicated in their conservative, non-integration economic policies by the fact that the country has thus far been relatively safe from the effects of the global financial crisis and that the government has been able to stash away over USD 130 billion in foreign currency reserves. But running budget deficits while the price of oil and gas plummets could force Bouteflika's government to make hard choices between continued spending on legacy projects or preserving the rainy day funds of the hydrocarbons regulation fund and the

country's external reserves. This is a particularly hard choice for a government wary of riots in a country where socioeconomic discontent boils over regularly into small-scale civil unrest.
PEARCE